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IN THE

Supreme Court of the United States

OCTOBER TERM, 1943

No. 122

MUSKEGON MOTOR SPECIALTIES COMPANY,
a Delaware Corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

To the Honorable Supreme Court of the United States:

Muskegon Motor Specialties Company, a Delaware corporation, petitioner herein, respectfully prays for a writ of certiorari to the United States Circuit Court of Appeals for the Sixth Circuit to review the decree and order entered in this case on April 13, 1943 (R. 207), (opinion 134 F. 2nd. 904, R. 208) shows as follows:

I. SUMMARY STATEMENT OF MATTER INVOLVED

The proceeding in the Circuit Court of Appeals was upon a petition to review a decision of the United States Board of Tax Appeals promulgated on November 4, 1941 determining deficiencies in income and excess profits taxes against petitioner for the year 1934 in the respective amounts of $5,596.51 and $2,035.10. The opinion of the Board of Tax Appeals is reported at 45 B. T. A. 551.

The petitioner corporation was organized in 1928 and acquired all the outstanding stock of two Michigan corporations, L. O. Gordon Manufacturing Company and Muskegon Motor Specialties Company (hereinafter called respectively Gordon and Muskegon-Michigan), which corporations shortly thereafter conveyed all of their property to the petitioner and were then liquidated and dissolved. The petitioner in computing its income and excess profits taxes for the year 1934 computed depreciation on the basis of cost to it of the assets so acquired by it, contending that the transaction was not a reorganization as defined in the applicable Revenue Act, but was a sale by the stockholders of Gordon and Muskegon-Michigan; and that in any event, an interest or control of 50 per centum of the property transferred did not, after the transfer, remain in the same persons or any of them (see Sec. 113 (a) (7) Revenue Act of 1934). The Commissioner of Internal Revenue computed the depreciation on the basis of the cost to the two corporations, former owners of said assets, contending that under the Revenue Act the transaction was a reorganization and that a 50 per centum inter-

est or control did so remain in the transferors. The Board of Tax Appeals sustained the Commissioner and the Circuit Court of Appeals affirmed the decision of the Board (R. 208, 134 F. 2nd 904). A detailed statement of the facts of the transaction is reserved for a more appropriate place in the brief in support of this petition.

II. BASIS UPON WHICH THIS COURT HAS JURISDICTION TO REVIEW THE JUDGMENT OF THE CIRCUIT COURT OF APPEALS

(a) This Honorable Court has jurisdiction to review the judgment of the Circuit Court of Appeals in this case under the provisions of Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925, 43 Stat. 938; Title 28, U. S. C. A. 347.

(b) The statutes of the United States involved in this proceeding are the Revenue Act of 1928, Sec. 112 (i) (1); the Revenue Act of 1932, Sec. 112 (i) (1), Sec. 113 (a) (7); the Revenue Act of 1934, Sec. 112 (g) (1) and (h), Sec. 113 (a) (7) and (12), Sec. 113 (b), Sec. 114 (a); Internal Revenue Code Sec. 113 (a) (7). See also G. C. M. 7472, C.B. IX-1, page 184, 191; the pertinent provisions of all of which are set forth in the brief annexed hereto (p. 13 to 17).

(c) The decree of the Circuit Court of Appeals for the Sixth Circuit now sought to be reviewed was entered by said Court on April 13, 1943 (R. 207), and is final and erroneous.

III. STATEMENT OF QUESTIONS PRESENTED

The general question presented is whether the petitioner, in computing its income and excess profits taxes for the year 1934, is entitled to compute depreciation of the depreciable property, acquired in the transaction above described, on the cost to it of such property; or whether it must use the basis of net unrecovered cost of such property to Gordon and Muskegon-Michigan. Involved in the foregoing are the following subordinate questions:

(a) Was the transaction by which the petitioner acquired the property of Gordon and Muskegon-Michigan a reorganization as that term is used in the applicable Revenue Act, or was it a sale or exchange?

(b) Who were the transferors of said property to the petitioner? Were they the Gordon and Muskegon-Michigan corporations or were they their stockholders?

(c) Was the transaction by which the petitioner acquired the stock and property a tax free transaction?

(d) After the transfer of said property to the petitioner did a 50 per centum interest in said property so transferred "remain in the same persons or any of them"?

(e) After the transfer of said property to the said petitioner, did a 50 per centum control of the property transferred "remain in the same persons or any of them"?

IV. REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT

(a) The decision of the Circuit Court of Appeals for the Sixth Circuit decides important questions of Federal law which have not been but should be settled by this Court.

(b) The Circuit Court of Appeals has decided Federal questions in a way probably in conflict with applicable decisions of this Court.

Wherefore, your petitioner prays that this Honorable Court will grant its writ of certiorari directed to the Circuit Court of Appeals for the Sixth Circuit, requiring the complete record of this cause in said Court to be certified to this Court and that this Court will thereupon proceed to correct the errors herein complained of.

And your petitioner will ever pray, etc.

MUSKEGON MOTOR SPECIALTIES COMPANY

By Hal H. Smith,
Counsel for Petitioner.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

THE OPINION OF THE COURT BELOW

The opinion of the Circuit Court of Appeals for the Sixth Circuit is reported at 134 F. 2nd. 904. The opinion of ~~February 13, 1925, 43 Stat. 938; Title 28, U. S. C. A. 551.~~

the Board of Tax Appeals is reported at 45 B.T.A. 551.

JURISDICTION

1. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925, 43 Stat. 938; Title 28, U. S. C. A. 347.

2. The decree of the Circuit Court of Appeals for the Sixth Circuit was entered on April 13, 1943 (R. 207). No petition for rehearing was filed.

3. The nature of the case, the rulings of the Circuit Court of Appeals for the Sixth Circuit, and the reasons relied upon why a writ of certiorari should be granted are set forth in the foregoing petition.

4. The grounds on which the writ is asked are two of the reasons set forth in Rule 38, 5 (b) of your Honorable Court, as follows:

(a) The decision of the Circuit Court of Appeals decides important questions of Federal law which have not been but should be settled by this Court, and

(b) The Circuit Court of Appeals has decided Federal questions in a way probably in conflict with applicable decisions of this Court.

STATEMENT OF THE CASE AND QUESTIONS INVOLVED

The questions involved were set forth in the petition and in the interest of brevity will not be repeated here. The summary statement in the petition of the matter involved must be here amplified by a fuller statement of the facts. These facts are as follows.

Prior to November 24, 1928, the L. O. Gordon Manufacturing Company (hereafter called Gordon) was a Michigan corporation, having an outstanding capital stock of 2,000 shares of a par value of $100.00 each. Of this capital stock L. O. Gordon owned 420 shares and Mrs. L. O. Gordon owned 120 shares. The remaining 1,440 shares were owned by other individuals.

Likewise, in 1928 Muskegon Motor Specialties Company (hereafter called Muskegon-Michigan) was a Michigan corporation, having outstanding 4,500-9/10th shares of no par stock. Of this capital stock Flanders Investment Company owned 2,228 shares and other stockholders owned 2,272-9/10th shares.

L. O. Gordon was president of Gordon, and F. L. Flanders was president of Muskegon-Michigan. These two men, over a period of ninety days preceding November 24, 1928, discussed and planned the organization of a new company (R. 53). Mr. Gordon interviewed the other stockholders of Gordon and procured options at various prices on their stock in that company.

On November 24, 1928, the petitioner, Muskegon Motor Specialties Company, a Delaware corporation, was organized with an authorized capital stock of 62,500 shares of

Class A Convertible Preference stock and 187,500 shares of common stock without par value (R. 57). The Class A stock carried a $2.00 per share per annum cumulative dividend. It is provided in the Certificate of Incorporation (R. 80) that in the event of any liquidation, dissolution or winding up of the corporation, the Class A stockholders should receive all dividends accrued or in arrears and that the remaining net assets should be divided among the holders of the Class A stock and the holders of the common stock, each share of Class A stock then outstanding to receive an amount equal to four times the amount distributed upon and in respect to each share of common stock then outstanding. The Class A stock was callable at the option of the company on any dividend date in whole or in part at $35.00 a share together with all accrued and unpaid dividends.

Each share of Class A stock and common stock was entitled to one vote for all purposes (R. 83-84).

The Certificate of Incorporation of petitioner also provides that "no sale, lease or exchange of all its property and assets, including its goodwill and its corporate franchise, as an entirety, shall be made except when it has been authorized by the affirmative vote of the holders of a majority of shares of each class of the capital stock of this corporation" etc. (R. 88), that the Class A stock can not be increased without the affirmative vote or consent of a majority of the holders of the Class A shares; and no stock having priority over or equality with the Class A stock can be issued without such affirmative consent.

On November 27, 1928 the petitioner made a financing agreement with a banking group for the sale to such group of the 62,500 shares of its Class A stock and 15,000

shares of the common stock, for a total consideration of $1,385,000.00 (R. 112). As a part of this agreement, the petitioner agreed to pay to the holders of the outstanding capital stock of Gordon and Muskegon-Michigan cash aggregating $1,445,000.00 and to issue to some of them 110,000 shares of its common stock, all in exchange for all of the outstanding stock of the two companies. The difference between the amount of cash received from the bankers and the amount of cash to be paid to the stockholders, as above, was $60,000.00. This $60,000.00 was to be provided out of a cash dividend which would be paid to petitioner by Gordon (R. 114).

The financing agreement provided also (R. 116) that the petitioner might, at any time after it had acquired the entire stock of Gordon and Muskegon-Michigan, cause one or both of those companies to convey their assets to the petitioner in consideration of the surrender and cancellation of the shares of the capital stock of the company or companies making such conveyance and the assumption of all outstanding liabilities of such company or companies by the petitioner. That thereupon Gordon or Muskegon-Michigan, as the case might be, might be dissolved.

No agreement was entered into between Gordon and Muskegon-Michigan or between the two companies on the one hand and the petitioner on the other. There was no reorganization plan ever prepared or signed. There was no inter-corporate action whatever.

On November 27, 1928 petitioner organized two subsidiaries under the laws of Delaware: Midland Investors, Inc. and Norton Securities Company. Midland had 5,000 shares of stock; Norton 3,750 shares of stock. Petitioner

subscribed and paid for the total stock of both of these companies, paying $225,000.00 for the shares of Midland and $375,000.00 for the shares of Norton. The Norton payment was all cash. The Midland payment was $165,000.00 in cash and an assignment of $60,000 out of the $60,004.17 dividend of Gordon. This was assigned on December 6, 1928 and the dividend was declared on December 7, 1928 (R. 29).

On December 6, 1928 the petitioner issued and delivered to the banking group the 62,500 shares of its Class A stock and 15,000 shares of its common stock, all for the sum of $1,385,000.00, as above (R. 59).

Mr. L. O. Gordon, having procured the options on the 1,440 shares of Gordon stock, which was the balance of the stock not owned by him and Mrs. Gordon, turned the options over to the petitioner (R. 152). The stockholders giving these options deposited their stock in escrow. The total amount called for in the options was $433,507.60 (R. 152). This amount the petitioner paid direct to the several Gordon stockholders and received their stock. The petitioner then paid Mr. Gordon and Mrs. Gordon for their 560 shares cash in the amount of $15,492.40 and the 5,000 shares of Midland taken at a value of $45.00 as share or $225,000.00 and delivered to them also 35,000 shares of its own common stock (R. 59).

Mr. F. L. Flanders, president of Muskegon-Michigan, on November 7, 1928 issued a letter to its stockholders advising of a plan for the creation of a new company and proposing an exchange of the shares of the stock of Muskegon-Michigan on the basis of a cash payment of $171.30 and the delivery of 16 2/3 shares of the common

stock of the new company, the petitioner, for each share of stock of Muskegon-Michigan. All the outstanding stock of Muskegon-Michigan was thereafter deposited by the stockholders with the Union National Bank of Muskegon to effectuate the proposed sale (R. 122). Again thereafter, Flanders Investment Company was paid $6,-652.23 in cash and 3,750 shares of Norton of the value of $375,000.00 (R. 71). There was also delivered to it 37,118 1/3 shares of petitioner's common. At the same time the other stockholders of Muskegon-Michigan were paid $389,347.77 in cash and 37,881 2/3 shares of petitioner's common stock was delivered to them (R. 71).

The cash and its equivalent paid for the stock of the two companies totalled, as aforesaid, $1,445,000.00 (R. 71).

From December 6, 1928, when the petitioner acquired all the shares of stock of both Gordon and Muskegon-Michigan, those companies became inactive. On January 23, 1929 petitioner, the then owner of all the stock of both these companies, caused them to be dissolved (R. 63; see also R. 177-180, 189, 190). On the same date Muskegon-Michigan and Gordon conveyed all of their assets to the petitioner (R. 180). In each case the notice of dissolution provided: "has been dissolved by the sale of all its property and assets to Muskegon Motor Specialties Company, a Delaware Corporation."

The stockholders of both Gordon and Muskegon-Michigan were assessed and paid an income tax liability on the difference between the amounts received by them and the cost to them of their several shares of stock. The taxable gain recognized to all the Muskegon-Michigan stock-

holders was $703,713.45 (R. 32); that of Mr. and Mrs. Gordon was $212,492.40 (R. 32); that of the other Gordon stockholders is not in the record, but it can be computed approximately (R. 152, 196). The total taxable gain of all Gordon-Michigan stockholders is at least $1,222,748.43.

The fair market value of the properties of Gordon and Muskegon-Michigan at the date of acquisition by the petitioner is stipulated (R. 61) to be: for Gordon, $377,362.85; for Muskegon-Michigan, $545,181.88; a total of $922,544.73. The Commissioner has heretofore determined that the net unrecovered cost as of December 31, 1928 of the Gordon assets was $214,675.51 and of the Muskegon-Michigan assets $23,369.62 (R. 61). It was stipulated that, if the petitioner's depreciation allowance is to be computed on the cost to the petitioner, then the cost basis as to the Gordon depreciable assets is $364,684.10 and on the Muskegon-Michigan assets $490,896.88, these amounts being the fair market values of such assets on the date of their transfer to the petitioner (R. 62-63). The amount of petitioner's cost basis which is denied it by the decision of the Circuit Court of Appeals is $617,535.84.

After the completion of the transaction above recited, the Class A stock of the petitioner was owned 100% by the bankers. The common stock of petitioner was owned as follows: bankers 12%; former Muskegon-Michigan stockholders 60%; L. O. Gordon and Mrs. Gordon, former Gordon stockholders, 28%. Flanders, who owned through the Flanders Investment Company 49% of Muskegon-Michigan before the transfer, owned approximately 30% of petitioner's common stock after the transfer. The other Muskegon-Michigan stockholders who owned

51% of Muskegon-Michigan before the transfer, owned approximately 30% of petitioner's common stock after the transfer. L. O. Gordon and Mrs. Gordon, who owned 28% of the Gordon stock before the transfer, owned 28% of petitioner's common stock after the transfer. Other Gordon stockholders, who before the transfer owned 72% of Gordon's stock, owned none of the petitioner's stock after the transfer, having been paid off in cash. All Gordon and Muskegon-Michigan stockholders who owned some of petitioner's common stock after the transfer owned a total of 110,000 shares of petitioner's total common stock of 125,000 shares of petitioner's total of Class A stock and common stock of 187,500 shares. The bankers, after the transfer, owned 12% of petitioner's common stock and all of petitioner's 62,500 shares of Class A stock.

STATUTES INVOLVED

The statutes involved are as follows: (included also are the sections and the memoranda of the General Counsel of the Department of Internal Revenue referred to herein):

Revenue Act of 1928, Sec. 112 (i) (1).

> (i) *Definition of Reorganization.*—As used in this section and sections 113 and 115—
>
> (1) The term "reorganization" means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in

control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected.

Revenue Act of 1932, Sec. 112 (i) (1)

(i) *Definition of Reorganization.*—As used in this section and sections 133 and 115—

(1) The term "reorganization" means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected.

Revenue Act of 1932, Sec. 113 (a) (7).

(7) *Transfers to corporation where control of property remains in same persons.*—If the property was acquired after December 31, 1917, by a corporation in connection with a reorganization, and immediately after the transfer an interest or control in such property of 50 *per centum* or more remained in the same persons or any of them, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made. This paragraph shall not apply if the property acquired consists of stock or securities in a corporation a party to the reorganization, un-

less acquired by the issuance of stock or securities of the transferee as the consideration in whole or in part for the transfer.

Revenue Act of 1934, Sec. 112 (g) (1).

(g) *Definition of Reorganization.* — As used in this section and section 113—

(1) The term "reorganization" means (A) a *statutory* merger or consolidation, or (B) *the acquisition by one corporation in exchange solely for all or a part of its voting stock: of at least* 80 *per centum of the voting stock and at least* 80 *per-centum of the total number of shares of all other classes of stock of another corporation; or of substantially all the properties of another corporation,* or (C) a transfer by a corporation of all or a part of its assets to another corporation is immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (D) a recapitalization, or (E) a mere change in identity, form, or place of organization, however effected.

Revenue Act of 1934, Sec. 112 (h).

(h) *Definition of Control.*—As used in this section the term "control" means the ownership of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of the corporation.

Revenue Act of 1934, Sec. 113 (a) (7).

(7) *Transfers to Corporation Where Control of Property Remains In Same Persons.*—If the property was acquired after December 31, 1917, by a corporation in connection with a reorganization, and immediately after the transfer an interest or control in such property of 50 per centum or more remained in the same persons or any of them, then

the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made. This paragraph shall not apply if the property acquired consists of stock or securities in a corporation a party to the reorganization, unless acquired by the issuance of stock or securities of the transferee as the consideration in whole or in part for the transfer.

Revenue Act of 1934, Sec. 113 (a) (12).

(12) *Basis Established by Revenue Act of* 1932. —If the property was acquired, after February 28, 1913, in any taxable year beginning prior to January 1, 1934, and the basis thereof, for the purposes of the Revenue Act of 1932 was prescribed by section 113 (a) (6), (7), or (9) of such Act, then for the purposes of this Act the basis shall be the same as the basis therein prescribed in the Revenue Act of 1932.

Revenue Act of 1934, Sec. 113 (b).

(b) *Adjusted Basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

Revenue Act of 1934, Sect. 114 (a).

(a) *Basis for Depreciation.*—The basis upon which exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall

be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property.

G. C. M. 7472, CB IX-1 page 184, 191.

> "The statute contains no definition of the meaning of the phrase 'interest or control in such property of 80 per centum or more.' The term 'control' in its ordinary connotation implies that which is unitary and in its nature indivisible and hence not capable of being expressed in terms of a percentage. • • •
>
> "The term 'interest' is a very broad one, clearly much broader than the term 'ownership.' • • • the conclusion is irresistible that the term in Section 204 (a) (7) is used to designate that ultimate or beneficial species of rights, in the nature of ownership, which the individual shareholder has in property the direct ownership of and the beneficial and legal title to which is in a corporation, of which the individual is a shareholder."

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred in the following respects:

1. In affirming the decision of the Board of Tax Appeals (45 B.T.A. 91).

2. In holding that the acquisition by petitioner of all the stock and all of the assets of Gordon and Muskegon-Michigan was a reorganization as that term is used in the applicable Revenue Act.

3. In holding that the acquisition by petitioner of all of the stock of Gordon and Muskegon-Michigan, which included full beneficial title to the assets thereof, for

$1,445,000.00 cash or its equivalent and 110,000 shares of petitioner's common stock of only a nominal value, was not a sale by the stockholders of Gordon and Muskegon-Michigan, but was instead a non-taxable exchange in a reorganization within the meaning of Section 112 (i) (1) (A) of the Revenue Act of 1928.

4. In holding that the real transferors of the assets of Gordon and Muskegon-Michigan were those corporations and not the stockholders thereof.

5. In holding that the transaction whereby petitioner acquired the stock of the two companies from the stockholders thereof and thereafter acquired the assets of said two companies was an intercorporate transaction rather than a transaction between petitioner and said stockholders.

6. In not holding that, if the transaction wherein the petitioner on December 6, 1928, acquired the stock of the two companies is to be separated from the transaction whereby petitioner on January 23, 1929, caused said two companies to be dissolved and their assets conveyed to it, then the latter transaction is a liquidating dividend and hence a taxable transaction.

7. In not holding that, before the cost basis to the Gordon and Muskegon-Michigan can be imputed to the petitioner under Section 113 (a) (7) of the Revenue Act of 1932 and Section 113 (a) (12) of the Revenue Act of 1934, it must appear that the petitioner acquired the property in a tax-free exchange in a reorganization.

8. In holding that immediately after the transfer an interest in the property transferred of 50 per centum or more "remained in the same persons or any of them."

In holding that immediately after the transfer an interest of 50 per centum or more in the Gordon assets "remained in the same persons or any of them."

In holding that immediately after the transfer an interest of 50 per centum or more in the Muskegon-Michigan assets "remained in the same persons or any of them."

9. In holding that the interests of stockholders of Gordon and Muskegon-Michigan in the assets intended for the new company can be added together (though Gordon stockholders have no interest in Muskegon-Michigan or vice versa) to make up a 50 per centum interest in or control of the property transferred and thus satisfy the requirement of Section 113 (a) (7) that such 50 per centum interest in or control of the property transferred "remained in the same persons or, any of them."

10. In holding that after the transfer a control in such property of 50 per centum or more "remained in the same persons or any of them."

In holding that immediately after the transfer a control of 50 per centum or more in the Gordon assets "remained in the same persons or any of them."

11. In holding that the "continuing interest" in the petitioner "represents a substantial part of the things transferred."

12. In holding that the voting stock received by the stockholders of Gordon and Muskegon-Michigan, the potential earnings thereof, the "voice in the management of petitioner and L. O. Gordon's presidency," all taken together, satisfy the requirement of the law and "represent a substantial part of the things transferred."

ARGUMENT

I. The decision of the Circuit Court of Appeals decides important questions of Federal law which have not been, but should be settled by this Court.

1. This Honorable Court has never defined the meaning of the word "control" as used in Section 113 (a) (7) of the Revenue Act of 1934.

2. It has never defined the meaning and the applicability of the word "control" as used in Section 113 (a) (7) of the Revenue Act of 1934 in a case where the stockholder transferors or the stockholders of the transferor corporations receive only common stock in the transferee corporation and that corporation has outstanding preference stock which has a certain control over the property transferred.

3. It has never defined the meaning and the applicability of the word "control" as used in the above section in a case where the transferor stockholders or the stockholders of the transferor corporation receive only common stock in the transferee corporation and that corporation has outstanding a preference stock, the consent of which must be secured before the corporation can sell, lease or exchange all its assets, which assets include the property transferred to it.

4. It has never defined the meaning and applicability of the word "interest" as it is used in Section 113 (a) (7) of the Revenue Act of 1934.

5. It has laid down no rule as to how interest should be computed with reference to Section 113 (a) (7), in a

case where the transferor stockholders or the stockholders of the transferor corporation or some of them receive 50 per centum or more of the voting stock of the transferee corporation, but that corporation has outstanding a preference stock which, on the liquidation, dissolution or winding up of that corporation, is entitled to more than fifty per cent of the assets thereof, which assets include the property transferred to it.

The Circuit Court of Appeals in its opinion holds that the fact that stockholders of the old corporations hold, after the transfer, more than 50 per centum of the common stock of petitioner, satisfies the requirement of the statute that an interest remain of 50 per centum in the property transferred, although on the liquidation, dissolution or winding up of the petitioner, less than said 50 per centum of that property would be distributed and go to said stockholders of the old corporations.

The Circuit Court of Appeals, in its opinion, holds that the fact that more than 50 per centum of the voting stock of petitioner is in the hands of some of the stockholders of the old corporations satisfies the requirement of the statute. That court gave no effect to the fact that the Class A stock of petitioner can prevent a sale, lease or exchange of all the assets of petitioner.

The question as to the definitions of "interest" and "control" and the meaning of these words in the statute applicable in the instant case is still a live question. The same words used in the same connection remain in the statute in Sec. 113 (a) (7) of the Internal Revenue Code.

II. The Circuit Court of Appeals has decided Federal questions in a way probably in conflict with applicable decisions of this Court.

A. The Circuit Court of Appeals held against the petitioner on its contention that, though the transaction fell within the literal language of the definition of a reorganization in Section 112 (i) (1) (A) of the 1928 and 1932 Acts, there must be a continuity of interest between the old and the new corporations on their stockholders and that the interest of the transferors in petitioner must represent a substantial part of the value of the things transferred (Opinion, R. 213). It held that both the Gordon and the Muskegon-Michigan stockholders had "a substantial stake" in the petitioner.

It is settled "that a transaction may not qualify as a 'reorganization' under the various revenue acts though the literal language of the statute is satisfied." *Gregory v. Helvering*, 293 U. S. 465; *Helvering v. Asphaltic Limestone Co.*, 62 S. Ct. R. 540.

In the present case there was no reorganization plan formulated. The old corporations, Gordon and Muskegon-Michigan, made no agreement either with the bankers or with petitioner. They took no part in any plan for reorganization. The transaction was between petitioner and the Gordon and Muskegon-Michigan stockholders who sold their stock to petitioner. The old companies never received any part of the consideration paid by the petitioner. They never distributed anything to their stockholders. The transfer of the assets by the old companies to petitioner, made after the purchase of all of their stock from the shareholders and after the old corporations had ceased business and had become inac-

tive, was but a mere formal act to confirm in petitioner the legal title of the assets, all beneficial rights in which had been acquired by it through the stock purchases.

It is an essential, if the transaction is held to be a reorganization, that the seller received an interest in the affairs of the transferee which "represented a material part of the transferred assets"

Helvering v. Minnesota Tea Co., 296 U. S. 378;

Pinellas Ice & Cold Storage Co. v. Commissioner, 287 U. S. 462;

Le Tulle v. Scofield, 308 U. S. 415.

In the *Minnesota Tea Co.* case the Court said:

> "And we now add that this interest must be definite and material; it must represent a substantial part of the value of the thing transferred."

The Circuit Court of Appeals apparently was of the opinion that it was sufficient here if the Gordon and Muskegon-Michigan stockholders received either a "substantial value" or if they had a "substantial stake" in petitioner. But the requirement is that the interest of the stockholders represents a "substantial part of the value of the thing transferred."

In computing the "stake" the Circuit Court of Appeals added together the voting stock received, the potential earnings (estimating these on the basis of those of the old companies), "the voice * * * in the management, and L. O. Gordon's presidency of petitioner."

The Court fixed no value for the common stock of petitioner received by some of the stockholders of the old companies and considered only its voice in the management.

Petitioner submits that these factors may assist in determining the *position* of the old stockholders in petitioner, but are not properly to be considered in determining continuity of interest or in settling whether "the interest of the transferors or their stockholders" does "represent a substantial part of the value of the thing transferred." Even if it were a question of the interest in the new corporation rather than in the thing transferred, that interest must be a proprietary interest.

Le Tulle v. Scofield, 308 U. S. 415.

Interest is linked with ownership. G.C.M. 7472 IX-1, Cum. Bulletin 184, 191 (1930), *Supra* p. 17.

In the present case at least the major proprietary interest in the assets of the petitioner is in the Class A stock, none of which is owned by any of the stockholders of the old corporations.

Can it be said that the 110,000 shares of the common stock of petitioner has a substantial interest in the assets transferred when on liquidation, it would receive only 29.3% of them, and although, with the Class A stock, it elects directors, still it cannot sell, lease or exchange the whole assets. We submit that to so hold is contrary to the theory of "continuity." "Continuity" is definitely tied to a much more substantial percentage of ownership. See the requirement under Section 113 (a) (B) Revenue Act of 1934 of an 80% ownership of all classes of stock.

Helvering v. Southwest Corporation, 315 U. S. 194.

The decision below does not square with that theory or with the cases, supra, which define continuity and emphasize its importance.

B. The Circuit Court of Appeals did not pass upon the question as to whether or not immediately after the transfer, an "interest" in such property of 50 per centum or more remained in the same persons or any of them. (Section 113 (a) (1) (7)). It did, however, hold that immediately after the transfer a "control" in such property of 50 per centum or more remained "in the same persons or any of them." It held that the use of the word "remained" connotes a continuity of control, that is, the existence of control, both before and after the transfer and that the existence of the necessary control before the transfer should be measured on the total stock held by the stockholders in both Gordon and Muskegon-Michigan, saying that:

> "Control remained in the stockholders of the transferee corporation if they had been owners of common stock in one of the transferor corporations, irrespective of the fact that they may or may not have been stockholders in both. If transferor stockholders, which includes those of Gordon and Muskegon-Michigan, collectively owned 50 per cent of the common stock of the new corporation, we think the statute is satisfied."

It held that if any of those persons who were stockholders in Gordon plus any who were stockholders in Muskegon-Michigan collectively controlled more than 50 per cent of the petitioner's stock immediately after the transfer, the statute was met.

The petitioner submits that if control is to "remain," it must mean that control existed before the transfer in some of the persons who had control after the transfer. The stockholders of petitioner did not control both Gordon and Muskegon-Michigan before the transfer. Flanders and other Muskegon-Michigan stockholders, who owned after

the transfer 75,000 common shares out of a total of 187,500 of both Class A and common, or 40%, owned prior to the transfer 100% of Muskegon-Michigan. But Mr. and Mrs. Gordon, who after the transfer owned 18 2/3% of petitioner's stock, owned only 28% of the Gordon stock before the transfer. Control of Gordon therefore before the transfer was not owned by the stockholders who had 18 2/3% of petitioner after the transfer. If, then, the word "remain" should be construed to mean that a control must have existed in these stockholders before the transfer, that is, a control of all the property transferred, it is clear that before the transfer, while Muskegon-Michigan stockholders in petitioner then controlled Muskegon-Michigan and its assets through their stock ownership, Mr. and Mrs. Gordon did not control Gordon or the assets owned by Gordon before the transfer.

The Circuit Court of Appeals held that the statute was satisfied if there was a common stock ownership of more than 50 per centum of the voting stock irrespective of the fact that the Class A stock could veto the action of the total voting stock if it assumed to sell, lease or exchange all the assets of the corporation.

This is apparently in conflict with the decisions of this Court which hold that it is effective, legal control of the property transferred that supplies the test laid down by the statute. There can hardly be effective legal control in any amount of the voting stock if it cannot, by its votes, completely control the property transferred. In *Handy & Harman v. Burnet*, 284 U. S. 136, this Court, in discussing the sections of the Revenue Act of 1918 having to do with consolidated returns of affiliated corporations, pointed out that control there meant 'legally enforceable'

control and said that control resting in considerations "having no binding force is not sufficient to satisfy the statute." The same rule should apply here.

It is respectfully submitted that for the foregoing reasons the writ of certiorari should be granted.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 122

MUSKEGON MOTOR SPECIALTIES COMPANY, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Board of Tax Appeals (R. 26–38) are reported at 45 B. T. A. 551. The opinion of the Circuit Court of Appeals (R. 208–215) is reported at 134 F. 2d 904.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered April 13, 1943 (R. 207). Petition for a writ of certiorari was filed June 28, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

The basic issue is whether the Commissioner correctly determined that the basis of the taxpayer's assets for depreciation is the same as the basis of those assets in the hands of its two predecessor companies. The issue turns upon the following questions:

1. Whether the taxpayer acquired the assets from the two predecessor companies in connection with a "reorganization," within the definition of Clause A of Section 112 (i) (1) of the Revenue Acts of 1928 and 1932.

2. Whether, immediately after such acquisition, "an interest or control in such property of 50 per centum or more remained in the same persons or any of them," as required by Section 113 (a) (7) of the Revenue Act of 1932.

STATUTES INVOLVED

Revenue Act of 1932, c. 209, 47 Stat. 169:

> SEC. 112. RECOGNITION OF GAIN OR LOSS.
>
> * * * * * *
>
> (i) *Definition of Reorganization.* — As used in this section and sections 113 and 115—
>
> (1) The term "reorganization" means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of an-

other corporation, or substantially all the properties of another corporation), * * *.

* * * * *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

* * * * *

(7) *Transfers to corporation where control of property remains in same persons.*—If the property was acquired after December 31, 1917, by a corporation in connection with a reorganization, and immediately after the transfer an interest or control in such property of 50 per centum or more remained in the same persons or any of them, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made. This paragraph shall not apply if the property acquired consists of stock or securities in a corporation a party to the reorganization, unless acquired by the issuance of stock or securities of the transferee as the consideration in whole or in part for the transfer.

* * * * *

Section 112 (i) (1) of the Revenue Act of 1928, c. 852, 45 Stat. 791, is identical with Section 112 (i) (1) of the Revenue Act of 1932.

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that —

* * * * *

(12) *Basis established by Revenue Act of 1932.*—If the property was acquired, after February 28, 1913, in any taxable year beginning prior to January 1, 1934, and the basis thereof, for the purposes of the Revenue Act of 1932 was prescribed by section 113 (a) (6), (7), or (9) of such Act, then for the purposes of this Act the basis shall be the same as the basis therein prescribed in the Revenue Act of 1932.

* * * * *

(b) *Adjusted Basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

* * * * *

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

(a) *Basis for Depreciation.*—The basis upon which exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property.

* * * * *

STATEMENT

Muskegon Motor Specialties Company (herein referred to as Muskegon Michigan) and the L. O. Gordon Manufacturing Company (herein referred to as the Gordon Company) were Michigan corporations engaged in the business of manufacturing cam shafts. Muskegon Michigan had outstanding 4,500.9 shares of no par value capital stock and the Gordon Company had outstanding 2,000 shares of $100 par value capital stock. (R. 26–27.) Flanders Investment Company, a personal holding company for Fred L. Flanders, president of Muskegon Michigan, owned 2,228 shares of the Muskegon Michigan stock (R. 30, 31). L. O. Gordon, president of Gordon Company, and his wife owned 560 shares of the Gordon stock. None of the Muskegon Michigan stockholders owned any shares of Gordon Company, and none of the Gordon Company shareholders owned any shares of Muskegon Michigan. (R. 29, 30.)

Under date of November 7, 1928, a circular letter was sent to the stockholders of Muskegon Michigan setting out a plan for the consolidation or merger of the two companies, stating that it had been "unanimously agreed upon by the officers and directors of both companies, by all the stockholders of L. O. Gordon Manufacturing Company, and by 96 percent of the stockholders of this Company, and is now submitted to the remain-

ing stockholders of this company for their approval." The plan, as set forth in the letter, called for the organization of a new corporation and provided (R. 27):

> In exchange for the shares of no par value stock now held by the stockholders of this company, there will be issued to said stockholders shares of Class B stock of said new or consolidated corporation on the basis of 16⅔ shares of said Class B stock for each share of no par value stock now issued and outstanding and in addition to said stock there will be paid to the holders of the no par value stock of the present company in cash the sum of $171.30 per share.

The letter solicited the deposit of their stock in escrow for the purpose of carrying out the plan, and all of the shares were deposited (R. 27).

Gordon obtained options to purchase the 1,440 shares of Gordon Company stock not owned by himself or his wife, for cash at various prices ranging from $150 to $322.58 per share. All the shares of this company were likewise deposited in escrow. (R. 27.)

The taxpayer was incorporated in Delaware on November 24, 1928. It had an authorized capital of 62,500 shares of no par class A convertible preference stock and 187,500 shares of no par common stock. The class A stock carried a $2 per share per annum cumulative dividend. It was entitled upon liquidation to a preference in the

amount of all dividend arrearages and thereafter to a distribution per share equal to four times the amount distributed upon each share of common outstanding. The class A stock was callable on any dividend payment date, in whole or in part of $35 per share, together with all accrued and unpaid dividends. Each share of class A and each share of common stock entitled the holder to one vote for all purposes. (R. 27–28.)

On November 27, 1928, the taxpayer entered into a financing agreement with a group of bankers. The bankers agreed to buy all of the class A stock and 15,000 shares of the common stock for $1,385,000 in cash. The taxpayer agreed to issue 110,000 shares of its common stock and to pay $1,445,004.17 to the holders of all the capital stock of Muskegon Michigan and the Gordon Company. The difference of $60,004.17 between the amount to be received from the bankers and the amount to be paid to the old stockholders was to be recouped by means of a dividend to be paid to taxpayer by the Gordon Company. It was further agreed that the taxpayer might at any time after acquiring the stock of Muskegon Michigan and the Gordon Company acquire their assets upon surrender of the stock. It was contemplated that this would be done as soon as practicable. (R. 28–29.)

The agreement was closed on December 6, 1928, and the taxpayer issued to the bankers the 62,500 of its class A and 15,000 of its common stock for

$1,385,000. On the same day taxpayer acquired all of the shares of Gordon Company and Muskegon Michigan. In return for the 560 Gordon Company shares directly held by L. O. Gordon and his wife, the taxpayer paid $240,492.40 in cash or its equivalent and issued 35,000 shares of its new common stock. The remaining shares were acquired for $433,507.60 in cash, pursuant to the options which Gordon assigned to the taxpayer. In return for the Muskegon Michigan shares held by Flanders Investment Company, the taxpayer paid $381,652.23 in cash or its equivalent,[1] and issued 37,118⅓ shares of its new common stock. The remaining shares were acquired for $389,347.77 in cash and 37,881⅔ shares of new common. (R. 29–30.)

Upon the completion of these transactions, the taxpayer owned all the outstanding stock of Gordon Company and Muskegon Michigan. All of the taxpayer's authorized capital stock was issued and outstanding except for 62,500 shares of common reserved for conversion of the class A. (R.

[1] The taxpayer, on November 27, 1928, had formed two subsidiaries, Midland Investors, Inc., and Norton Securities Company, paying $225,000 for all the stock of Midland and $375,000 for all the stock of Norton. The market values of the shares of these subsidiaries on December 6, 1928, were $225,000 and $375,000, respectively. The payments to Mr. and Mrs. Gordon were in the form of $15,492.40 in cash plus all the shares of Midland. The payments to Flanders Investment Company were in the form of $6,652.23 in cash and all the shares of Norton. (R. 29–30.)

30.) Flanders, who had spoken for the stockholders of Muskegon Michigan, became chairman of the board and treasurer of the taxpayer. Gordon, who had represented the Gordon Company stockholders, became president. (R. 31–32.) Gordon Company and Muskegon Michigan were inactive after the taxpayer's acquisition of the stock, and were legally dissolved on January 23, 1929 (R. 31).

The aggregate cost to the taxpayer of the depreciable assets acquired in the transaction, measured by their market value at the time of acquisition, was $855,580.98. The adjusted basis of the assets in the hands of the two predecessor companies aggregated $238,045.14. (R. 32.)

The Board sustained the Commissioner's determination that the taxpayer must use the basis of the predecessor companies in computing depreciation (R. 33–38). The court below affirmed (R. 207–215).

ARGUMENT

Section 114 (a) of the Revenue Act of 1934, *supra,* provides that the basis for computing the depreciation allowance upon property "shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property." Section 113 (b) provides that the "adjusted basis for determining the gain or loss from the sale or other disposition of property * * * shall be the

basis determined under subsection (a)," with adjustments not here material. Section 113 (a) provides that "The basis of property shall be the cost of such property," with certain exceptions thereafter specified.

The Commissioner's position rested upon the exception to the basis of cost specified in Section 113 (a) (12). This section provides that if property was acquired prior to 1934—

> and the basis thereof, for the purposes of the Revenue Act of 1932 was prescribed by section 113 (a) (6), (7), or (9) of such Act, then for the purposes of this [the 1934] Act the basis shall be the same as the basis therein prescribed in the Revenue Act of 1932.

Section 113 (a) (7) of the Revenue Act of 1932, *supra,* provides that if property was acquired—

> by a corporation in connection with a reorganization, and immediately after the transfer an interest or control in such property of 50 per centum or more remained in the same persons or any of them, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made. * * *

The term "reorganization" is defined in Section 112 (i) (1) (A) of both the 1928 and the 1932 Acts, to mean, *inter alia*—

> a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation) * * *.

The taxpayer's contentions are twofold. First, the taxpayer argues that although the transaction comes within the literal definition of a reorganization contained in Clause A of Section 112 (i) (1), the stockholders of the predecessor companies did not retain the substantial interest in the transferred assets required for a reorganization under *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378; *Pinellas Ice Co.* v. *Commissioner*, 287 U. S. 462; and *LeTulle* v. *Scofield*, 308 U. S. 415. Secondly, the taxpayer argues that even if the property was acquired in connection with a reorganization, the bases of the transferor companies will not carry over because there was lacking the retention of the 50% interest or control required by Section 113 (a) (7).[2] We submit, however, that both

[2] The requirement is no longer present in the statutes with respect to reorganizations taking place in taxable years beginning after December 31, 1935. Revenue Act of 1936, Section 113 (a) (7), as amended by the Revenue Act of 1938, c. 289, 52 Stat. 447, Section 807; Revenue Act of 1938, Section 113 (a) (7); Internal Revenue Code, Section 113 (a)

points were correctly decided against the taxpayer, and that there is no occasion for further review.[3]

The first point involves the application of a familiar rule to the particular facts of the instant case. Stockholders of the old companies received all except 12% of the outstanding common stock of the new company. Muskegon Michigan stockholders received 60%; Gordon and his wife, 28%. The common was subject to the class A's annual dividend preference of $125,000, but as the court below pointed out (R. 212), the combined earnings of the two predecessor companies for the prior three years averaged over $240,000 annually. The common, moreover, had equal voting rights, share for share, with the class A, and hence voting control. The court below concluded that these common shares constituted a substantial stake in the taxpayer in view of the potential earnings attributable to them and the voice in the management which the shares represented. Contrary to the taxpayer's apparent contention (Br. 24), neither the added participation of the class A on liquidation nor the fact that the taxpayer's charter con-

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(7); H. Rep. No. 1860, 75th Cong., 3d Sess., p. 32 (1939–1 Cum. Bull. (Part 2) 728, 751.)

[3] The taxpayer has not repeated in its supporting brief the argument, advanced in the court below and also rejected, that upon carry-over of the bases of the predecessor companies an adjustment should be made for the gain on the transaction realized by the individual stockholders. The lack of merit in the contention is clearly shown in the opinion below (R. 215).

tained the customary provision for a class vote on a sale, lease or exchange of all the assets, compels a different conclusion.

The taxpayer's argument on the second point is that although former stockholders of Muskegon Michigan and Gordon Company collectively owned more than 50% of the taxpayer's voting stock immediately after the transfer, the control requirement of Section 113 (a) (7) was not satisfied since Mr. and Mrs. Gordon, the stockholders of Gordon Company who continued to hold a stock interest in the enterprise, only owned 28% of the Gordon Company stock prior to the transfer.[4] As the court below pointed out, however (R. 213–214), the statute only requires that control remain "in the same persons or any of them." Even if we assume, therefore, that Mr. and Mrs. Gordon were not in control of Gordon Company before the transfer, plainly they are within the phrase "any of them."[5] See *Fairbanks Court W. Groc. Co.* v.

[4] The Board of Tax Appeals, it should be observed, had concluded that Gordon, by virtue of the options he had obtained, had become the owner of all the stock of Gordon Company (R. 37).

[5] The court did not pass on the question whether the former stockholders had retained a 50 percent "interest" as well as "control." It is sufficient, of course, if *either* is present. See *Palm Springs Corp.* v. *Commissioner*, 315 U. S. 185, 187–188, fn. 1; *Bickford's, Inc.* v. *Helvering*, 98 F. 2d 568, 569 (C. C. A. 2d). The *Bickford* case also points to the difference, noted by the court below, between the meaning of the term "control" in Section 113 (a) (7) and the meaning of that term as it is specifically defined for the purposes of Section 112 of the Act.

Commissioner, 84 F. 2d 18, 19–20 (C. C. A. 7th), certiorari denied, 299 U. S. 582. The suggestion that ownership of over 50% of the voting stock of the company did not represent "control" within the meaning of Section 113 (a) (7) in view of the class A's veto power on the sale, lease, or exchange of the assets seems plainly without merit.

There is no conflict.

CONCLUSION

The petition for certiorari should be denied.

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JULY 1943.

U. S. GOVERNMENT PRINTING OFFICE: 1943

IN THE

Supreme Court of the United States

OCTOBER TERM, 1943

No. 122

MUSKEGON MOTOR SPECIALTIES COMPANY,
Petitioner,

v.

GUY T. HELVERING, Commissioner of Internal Revenue
Respondent.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit

REPLY BRIEF TO BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

A short reply to the brief for the respondent in opposition to the petition for writ of certiorari in the above entitled matter may be proper.

The Government makes no answer to our contention that the Circuit Court of Appeals has decided an important question of federal law which has not been but which should be decided by this court. It states only that it is rightly decided.

The statement on page 11 of the brief for the respondent in respect to the taxpayer's contentions as to the

issues involved in the case is not precise. The first contention as stated is correct. The taxpayer, however, also contends that the transaction involved was not an intercorporate transaction and so not a reorganization (Specification of errors 2, 4 and 5, page 18, of petitioner's brief). The reorganization provisions of the statute are restricted to intercorporate transactions. *Helvering v. Cement Investors*, 316 U. S. 527.

In this connection it is contended that the real transferors of the property were the Gordon and Muskegon-Michigan stockholders and not the Gordon and Muskegon-Michigan companies. Respondent's brief makes no answer to this.

It is also contended that the transaction was not a tax-free transaction. No reply is made to this except to claim that petitioner has not repeated in its brief the contention made below that an adjustment for the gain realized by the individual stockholders. Obviously, if the real transferors are the stockholders and they paid a tax on a profit of upwards of $1,222,000.00, the bases should be increased.

The second statement as to petitioner's contention is correct. The petitioner does contend that, assuming that the transaction was intercorporate, 50% control did not remain in the same persons or any of them, and also 50% interest did not remain in the same persons or any of them.

On page 7 of respondent's brief appears the following:

> "The taxpayer agreed to issue 110,000 shares of its common stock and to pay $1,445,004.17 to the

> holders of all the capital stock of Muskegon-Michigan and the Gordon Company."

It might be inferred from this that all of the stockholders of both companies not only received some cash, but also that all of them received some of the 110,000 shares of common stock. This is not the fact. Fourteen hundred forty shares of Gordon Company, or 72% of that company's total shares received no stock whatever and received nothing but cash. This error is emphasized again on page 12 of the brief by the following statement:

> "Stockholders of the old companies received all except 12% of the outstanding common stock of the new company."

While this does not say that all the stockholders of the old companies received common stock, it nevertheless may imply that they so did.

The statement by counsel in the note on page 11 of his brief that the requirement of 50% interest or control "is no longer present in the statutes," etc., is correct if it means no more than that this clause has been stricken from Section 113 (a) (7), insofar as being applicable to property acquired in a reorganization after December 31, 1935. But the inference which may be sought to be drawn from this note is that, since the later statutes eliminate the 50% clause, its proper construction is not of any importance. This is not true. The clause is still applicable in respect to all reorganizations in which property was acquired after December 31, 1917, and before January 1, 1936. It will operate in the determination of depreciation and of gain or loss in case of the sale of any such property at any time in the future. Its meaning and construction are therefore still of major importance.

CONCLUSION

We, submit therefore, that the brief of respondent makes no answer or reply to the following contentions made by us:

1. That this was not a reorganization because it was not an intercorporate transaction, but was a transaction between the stockholders of Gordon and Muskegon-Michigan individually and Petitioner and that neither Gordon nor Muskegon-Michigan were a party to any reorganization.

2. That the real transferors of the property were the stockholders of Gordon and Muskegon-Michigan and that, therefore, the basis should be increased in the amount of gain recognized to these transferors.

3. That Petitioner did not acquire the property in a tax-free exchange or non-taxable transaction and hence the transferor basis is not applicable but must be increased by the amount of gain recognized to the transferor.

4. That before the transfer Mr. and Mrs. Gordon had only a 28% interest in the Gordon assets and none in the Muskegon-Michigan assets. They had a smaller percentage after the transfer, and hence neither before nor after the transfer did 50% interest or control remain in them or any of them. The other Gordon stockholders received cash only and no stock.

5. That before the transfer the Muskegon-Michigan stockholders had no stock in the Gordon Company or other

interest in the Gordon assets and after the transfer they did not have a 50% interest or control in either the Gordon assets or the Muskegon-Michigan assets and that, therefore, an interest or control in the property of 50% or more did not remain in them or any of them.

6. That the foregoing and other questions raised by petitioner are important questions of federal law which have not been but should be decided by this Court.

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